



TEXAS

"Texas' economy was in better shape at the end of the second quarter than the first. Unemployment inched down while job growth continued in June, albeit at a slightly slower pace than the previous month. The energy sector's payrolls contracted for the fourth consecutive month, although oil prices rallied considerably. The service sector, while still lagging behind pre-pandemic employment levels, added 228,600 jobs. Real retail sales were only half a percent lower than all-time-high levels at the start of the year. Commodity exports, however, remained diminished. In comparison, housing sales rebounded 30 percent and are on track to make a full recovery in July. The Real Estate Center's Texas weekly leading economic activity index also projected continued improvement, but the path of recovery could be hindered by possible upsurges in COVID-19 cases." – Aug 2020 – Outlook for Texas Economy – Real Estate Center – Texas A&M University

AUSTIN

"The Austin economy showed signs of improvement in June following the impact of COVID-19. The Austin Business-Cycle Index surged. While employment and the unemployment rate improved in June from May, both remain significantly below their February levels. Consumer spending has improved considerably since mid-April in Travis County. While existing-home sales increased sharply in June, building permits declined." – Aug 2020 – Austin Economic Indicators – Dallas Fed

UNITED STATES

"Payroll employment increased at a slower pace in July. The unemployment rate fell, mainly due to a decline in temporary layoffs. The labor force participation rate was essentially unchanged and the employment-to-population ratio increased moderately; both were still low.

Consumer spending continued to rebound in June. Housing activity continued to recover in June. Real business equipment spending plunged in 2020 Q2.

Core PCE inflation remained well below the FOMC's longer-run objective. U.S. equity indices rose over the last month. Implied volatility decreased. Oil prices rose modestly." – Aug 2020 – U.S. Economy in a Snapshot – NY Fed

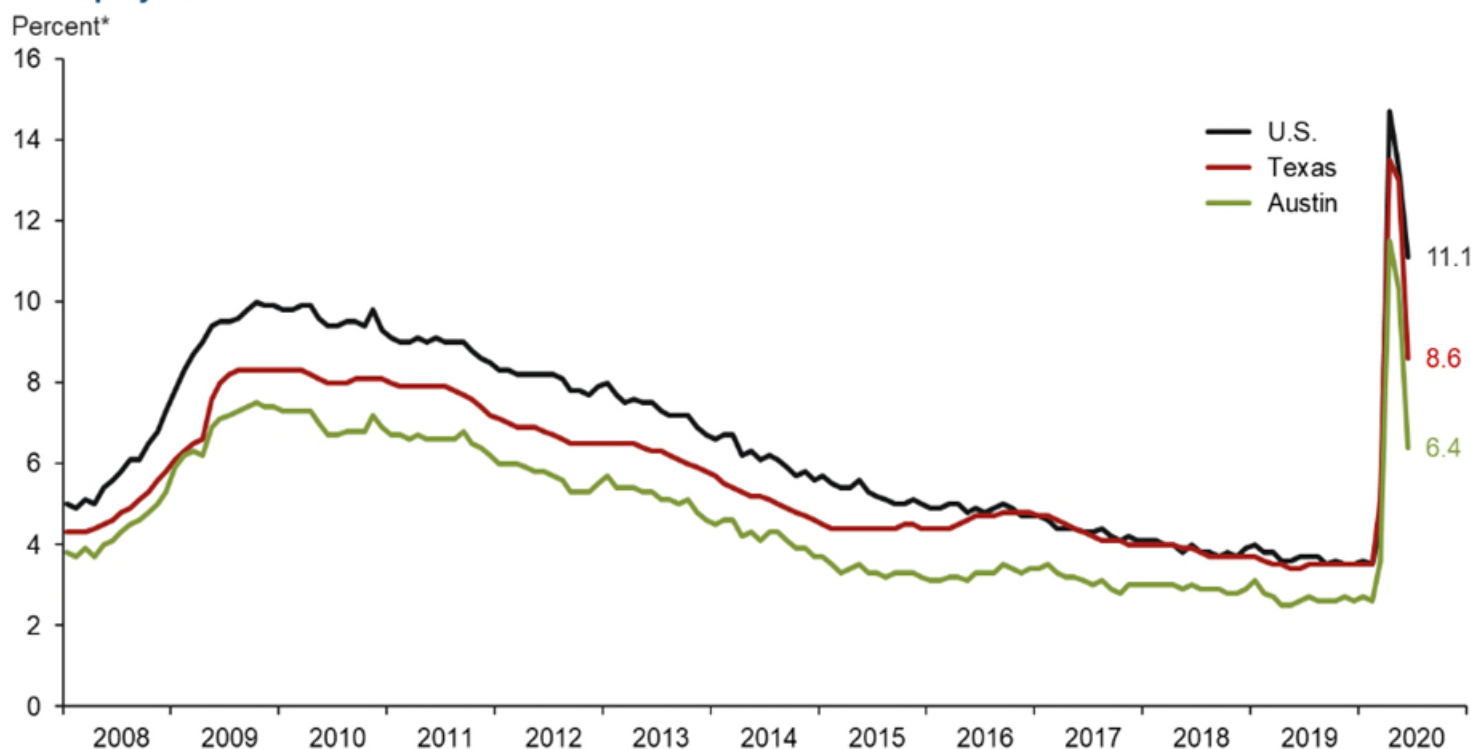
JOBS - UNEMPLOYMENT RATES – AUSTIN MSA, TEXAS, U.S.

“Austin’s [seasonally adjusted] unemployment rate fell to a still-elevated 6.4 percent in June. The jobless rate ticked down to 8.6 percent in the state and 11.1 percent in the nation.” – Aug 2020 – Dallas Fed

“The number of unemployed Americans dropped by 3,235,000 last month, and the nation’s unemployment rate also dropped to 11.1 percent, down from 13.3 percent in May and the record 14.7 percent in April.”

“Among the major worker groups, the unemployment rates declined in June for adult men (10.2 percent), adult women (11.2 percent), teenagers (23.2 percent), Whites (10.1 percent), Blacks (15.4 percent), and Hispanics (14.5 percent). The jobless rate for Asians (13.8 percent) changed little over the month.” – Jul 2020 – cnsnews

Unemployment Rate



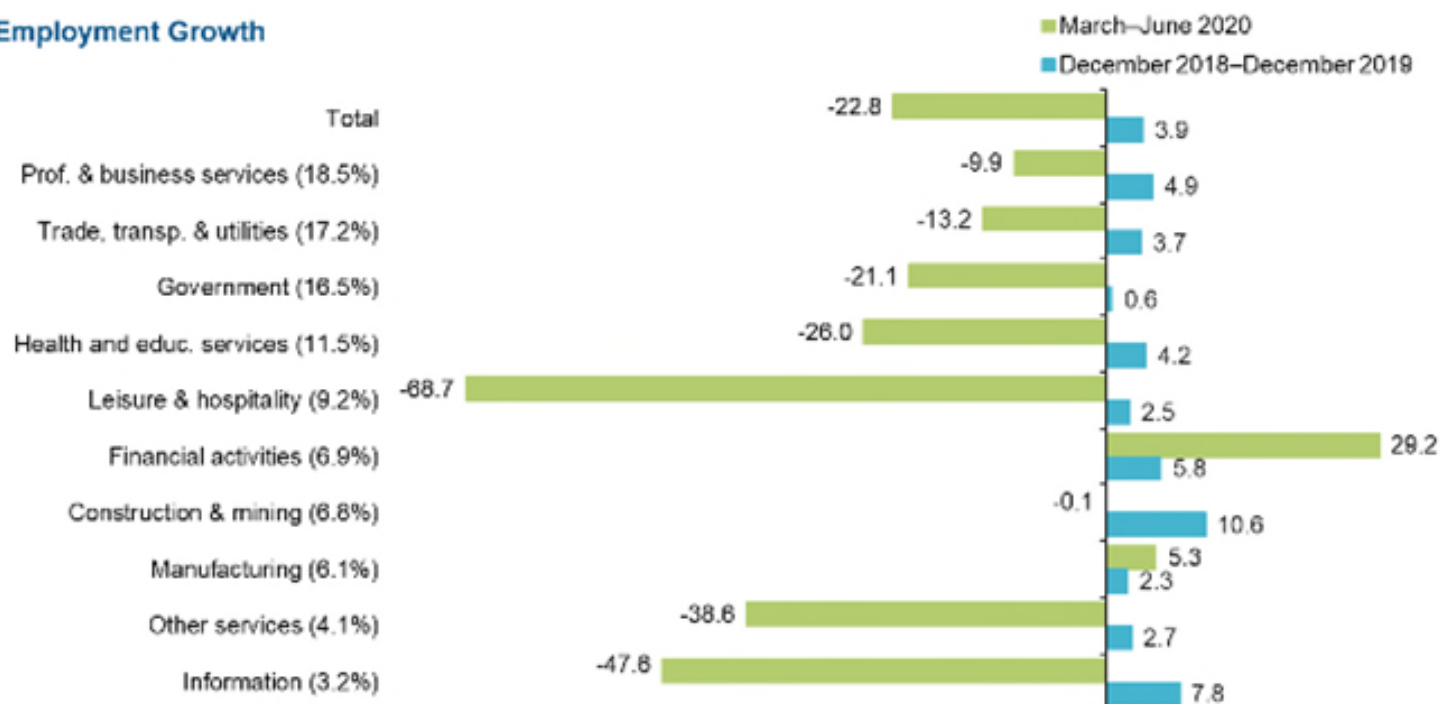
*Seasonally adjusted.
SOURCE: Bureau of Labor Statistics.

Provided by Federal Reserve of Dallas – Austin Economic Indicators – Aug 2020

JOBS – EMPLOYMENT GROWTH RATE – AUSTIN

“Austin payrolls contracted an annualized 22.8 percent (-71,020 net jobs, non-annualized) in the three months ending in June. All sectors other than manufacturing and financial activities shed jobs during this period. Leisure and hospitality plunged 68.7 percent, losing the most jobs (-32,820). It was followed by information, which contracted 47.6 percent (-5,950). Other services, such as automotive repair and barber shops, declined 38.6 percent (-5,600), health and private education services fell 26.0 percent (-9,560), and the government sector contracted 21.1 percent (-10,700). The financial activities industry saw a 29.2 percent gain, adding 4,600 jobs, and employment in the manufacturing sector grew 5.3 percent (840).” – Aug 2020 – Dallas Fed

Employment Growth



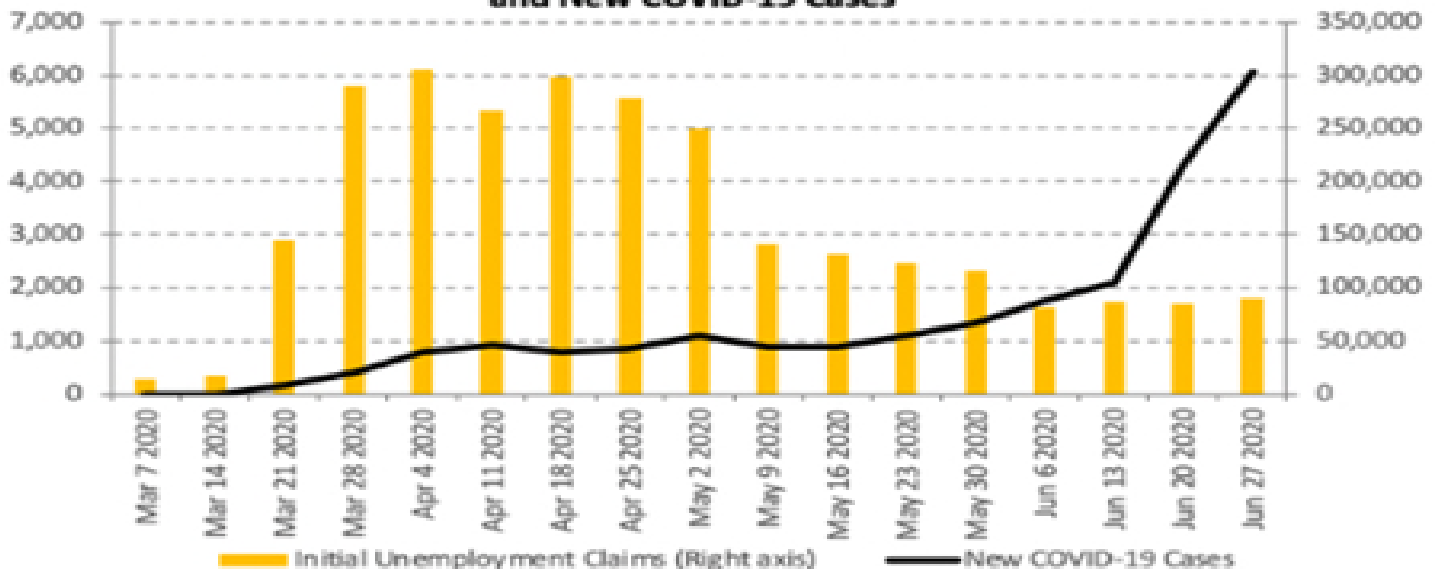
NOTE: Data show seasonally adjusted and annualized percentage employment growth by industry. Numbers in parentheses represent the share of total employment and may not sum to 100 due to rounding.

SOURCE: Bureau of Labor Statistics; Texas Workforce Commission; adjustments by the Dallas Fed.

JOBS – MAJOR TEXAS METRO WEEKLY UNEMPLOYMENT CLAIMS

“The number of Texans filing initial unemployment insurance claims decreased to 372,200, the lowest number of claims since February, but ticked up the last week of June amid rising new COVID-19 cases. (Fig 1 & 2) A backslide in economic activity due to a resurgence in new COVID-19 cases may trigger renewed joblessness. Meanwhile, average weekly continued unemployment insurance claims flattened...” – Aug 2020 – Outlook for the Texas Economy

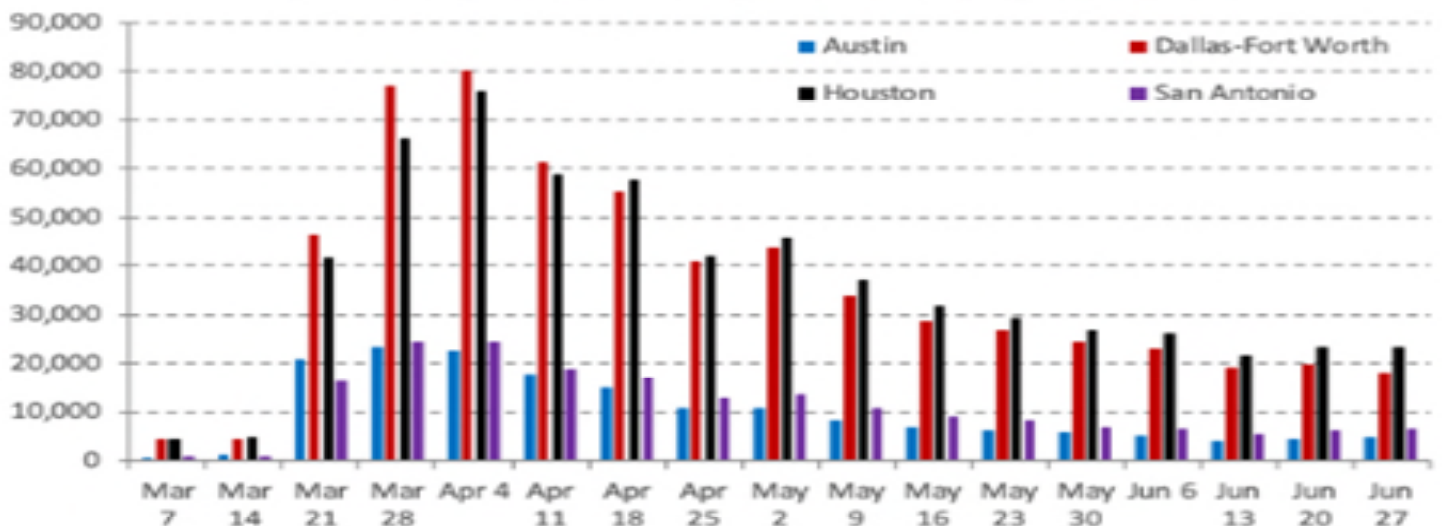
Figure 1. Texas Weekly Initial Unemployment Claims and New COVID-19 Cases



Note: Initial unemployment claims are seasonally adjusted.

Sources: Texas Workforce Commission, U.S. Department of Labor Employment and Training Administration, Real Estate Center at Texas A&M University calculations, and <https://github.com/nytimes/covid-19-data/blob/master/us-counties.csv>

Figure 2. Major Metro Weekly Initial Unemployment Claims



Note: Seasonally adjusted.

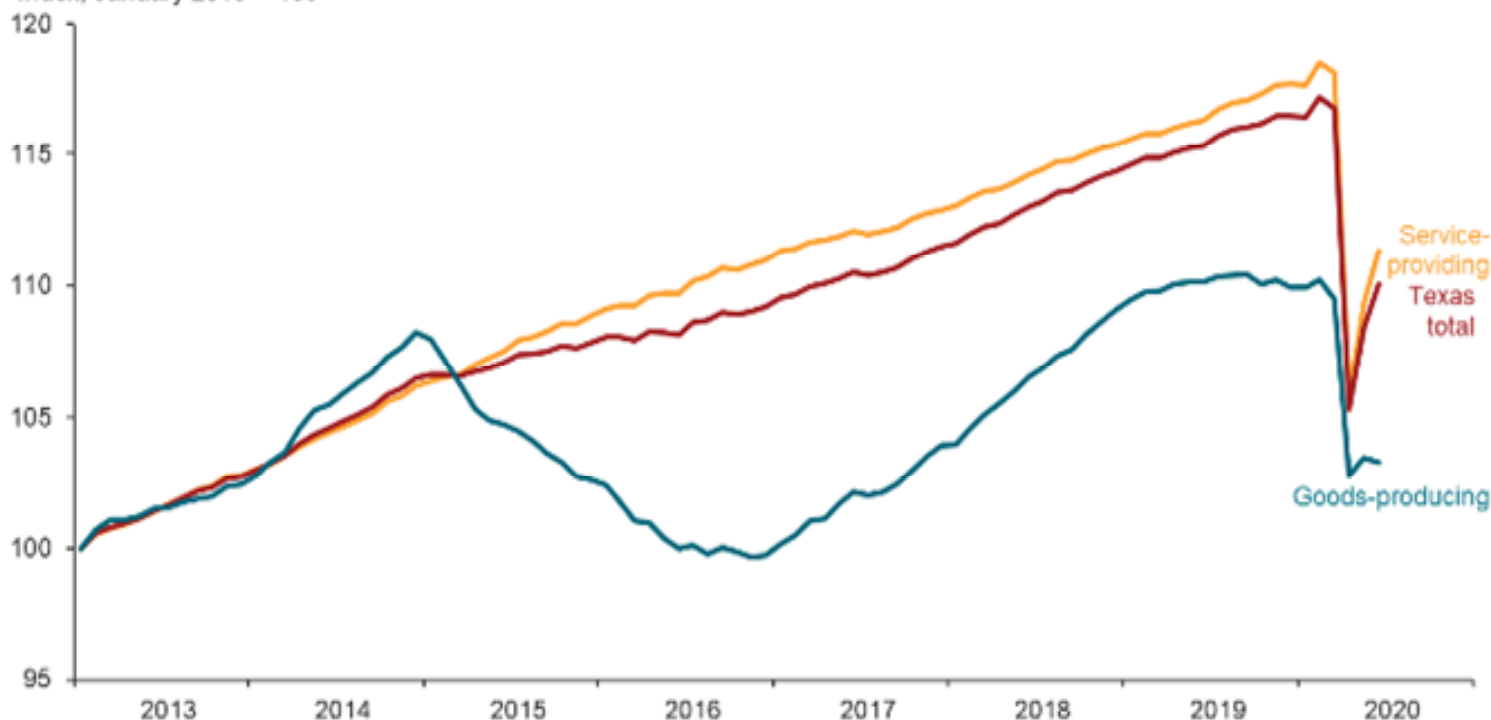
Sources: Texas Workforce Commission, U.S. Department of Labor Employment and Training Administration, and Real Estate Center at Texas A&M University calculations

JOBS – TEXAS SERVICE SECTOR JOB RECOVERY

“Texas employment grew a non-annualized 1.5 percent in June after upwardly revised growth of 2.9 percent in May. Texas employment has partially recovered since plummeting in March and April, with growth concentrated in the service-providing sector. Still, service-providing employment in June was 6.1 percent below its peak in February. **The recent growth suggests that many service-sector workers who were laid off or furloughed in March and April were back to work in May and June. High-frequency data suggest that this trend is reversing as establishments reduce capacity or close again following a statewide surge in COVID-19 cases and hospitalizations.** Employment in the goods-producing sector saw a less-severe decline in April, followed by weak growth in May and a slight contraction in June. Goods-producing employment in June was 6.3 percent below its peak in February.” – Jul 2020
– Texas Economic Indicators – Dallas Fed

Employment Growth by Sector

Index, January 2013 = 100*



*Seasonally adjusted.

SOURCE: Bureau of Labor Statistics; Texas Workforce Commission; adjustments by the Dallas Fed.

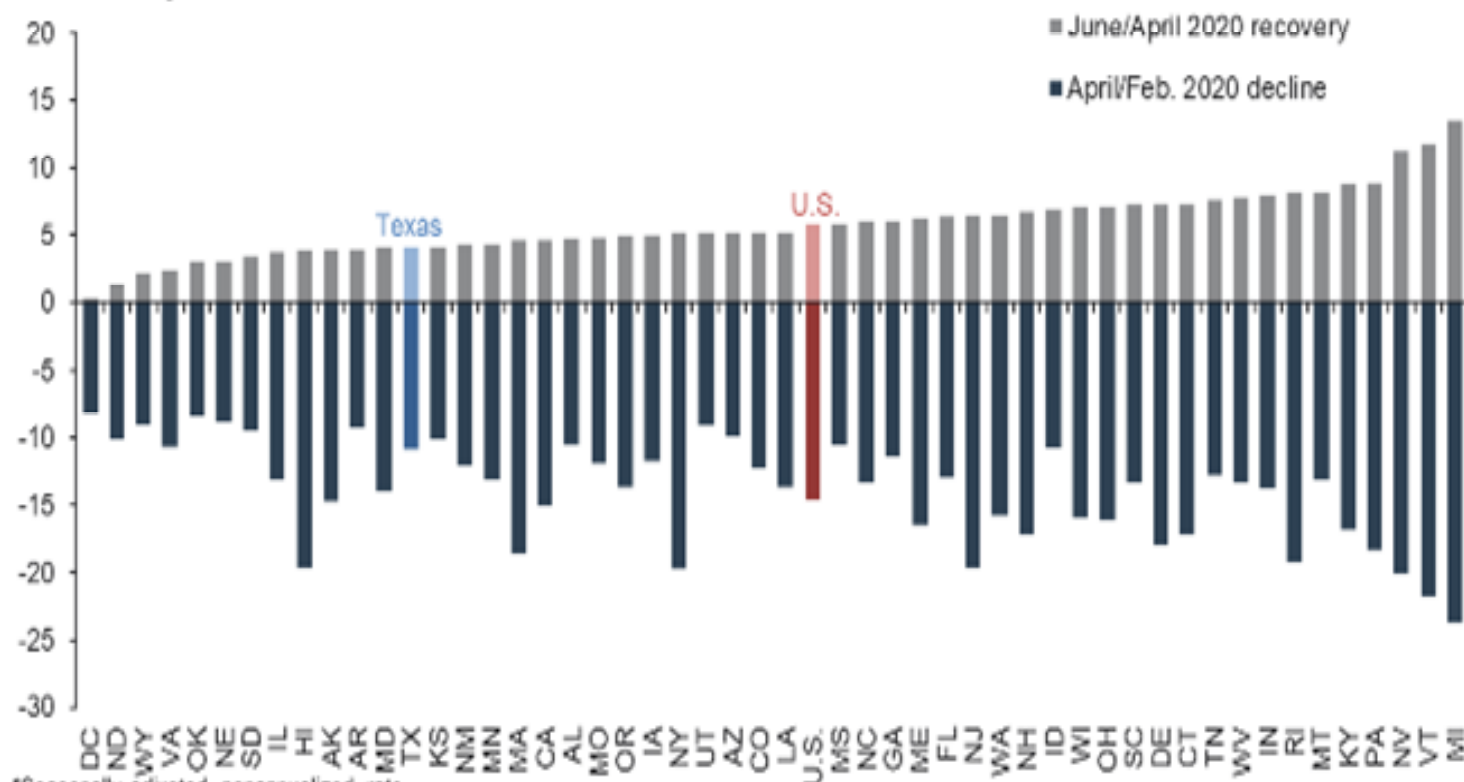
Provided by Federal Reserve of Dallas – Texas Economic Indicators – July 2020

JOBS – TEXAS EMPLOYMENT GROWTH

“Employment contracted in Texas from February to April, though declines were less severe compared with other states. After the two-month decline, **Texas’ job recovery from April through June has been slower than the national average.** Most of the country saw a similar pattern of contraction and growth from February to June, outside of Hawaii and the District of Columbia, where employment fell in May.” – Jul 2020 – Texas Economic Indicators – Dallas Fed

Employment by State

Percent change*



*Seasonally adjusted, nonannualized rate.

NOTE: Bar below zero for each state shows employment decline from February to April 2020. Bar above zero shows recovery from April to June 2020. For comparison purposes, the Bureau of Labor Statistics (BLS) Texas data are shown here without the usual adjustments by the Dallas Fed.

SOURCE: BLS.

Provided by Federal Reserve of Dallas – Texas Economic Indicators – July 2020

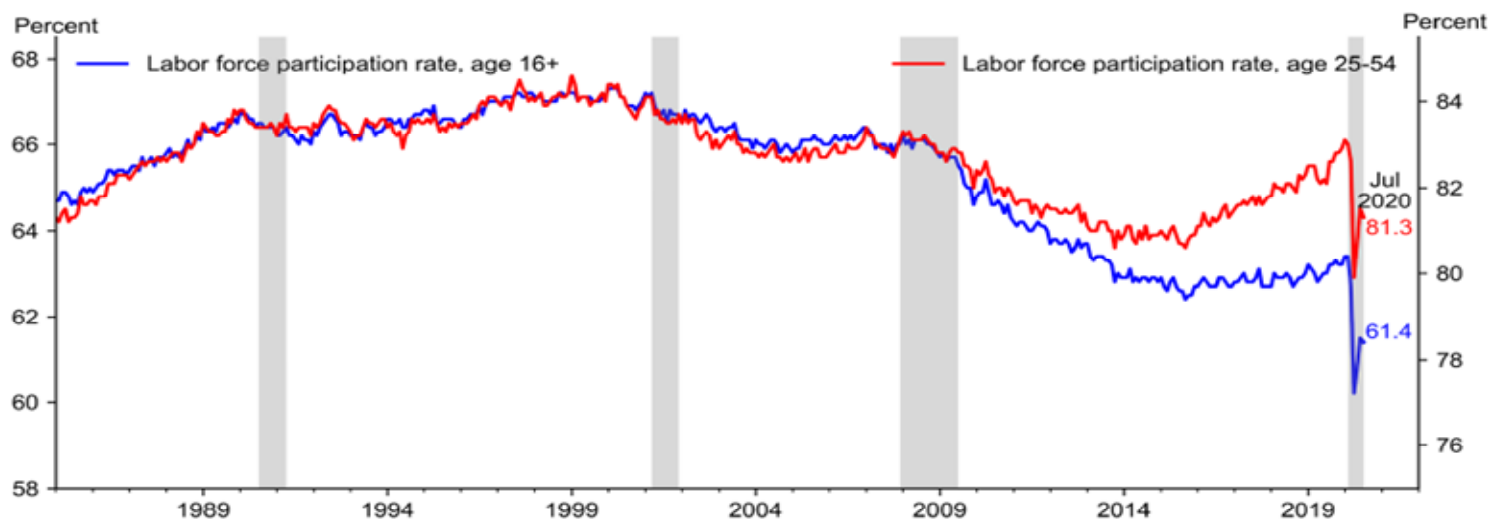
JOBS – LABOR PARTICIPATION RATE IN THE U.S.

“On Friday, the Labor Department's Bureau of Labor Statistics said the employment picture continues to improve, as 143,532,000 people were working in July, up 1,350,000 from the 142,182,000 employed in June. **This is the third straight monthly increase in the number of employed, although it's a smaller increase than June's (+4,940,000) and the one in May (+3,827,000).**”

“**The number of unemployed Americans** -- those who do not have a job but who have actively looked for work in the prior four weeks -- fell for a third straight month, to **16,338,000**, which compares with the 17,750,000 people counted as unemployed in June; 20,985,000 in May; and 23,078,000 in April. **Prior to the pandemic, this number hovered in the 5.7 - 5.8 million range.**”

“159,870,000 were participating in the labor force, meaning they either had a job or were actively seeking one during the last month. This resulted in a labor force participation rate of 61.4 percent, down a tenth of a point from 61.5 percent in June, and well below the Trump-era high of 63.4 percent set this past January and February.” – Aug 2020 – cnsnews

Labor Force Participation



SOURCES: Bureau of Labor Statistics.

Provided by Federal Reserve of Dallas – U.S. Economy Charts – Aug 2020

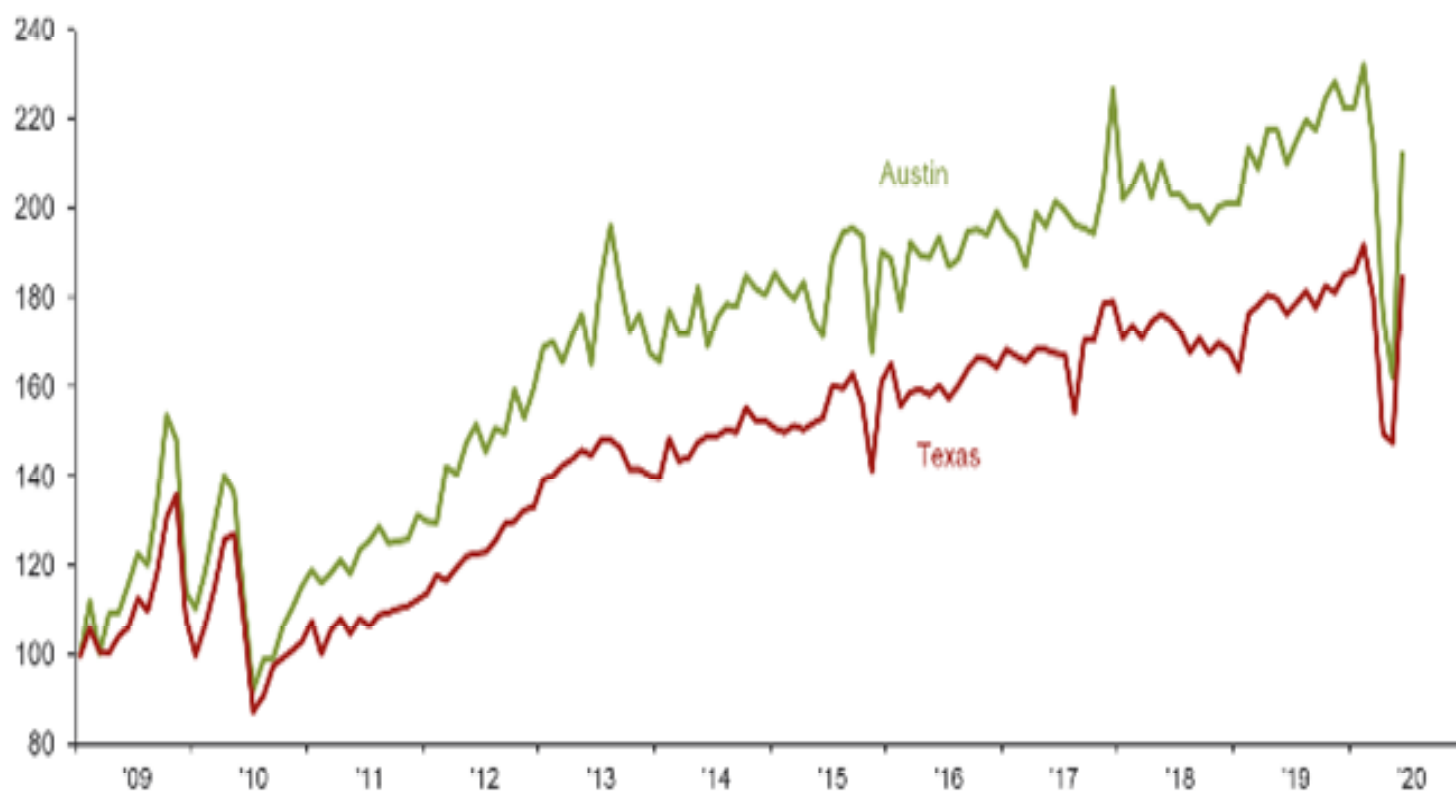
The **labor force participation rate**, as defined by the Bureau of Labor Statistics (BLS), is “the percentage of the population [16 years and older] that is either employed or unemployed [that is, either working or actively seeking work].” “A lower labor force participation rate is associated with lower gross domestic product (GDP) and lower tax revenues. It is also associated with larger federal outlays, because people who are not in the labor force are more likely to enroll in certain federal benefit programs” – Congressional Budget Office

HOUSING – EXISTING HOME SALES – AUSTIN MSA

“Existing-home sales in June climbed 31.1 percent in Austin and 25 percent in Texas. Nonetheless, the metro’s home sales were down 3.9 percent during the first half of the year relative to the same period in 2019 due to COVID-19-related containment measures, while Texas sales were down 1.5 percent. **The median price of homes sold in June was \$324,208 in the metro, a 3.9 percent gain year over year,** compared with \$248,852 in Texas, a 3.4 percent increase.” – Aug 2020 – Austin Economic Indicators – Dallas Fed

Existing-Home Sales

Index, January 2009 = 100*



*Seasonally adjusted.

NOTE: Data measure sales of residential units (single family, condominiums and townhomes).

SOURCE: Multiple Listing Service; Real Estate Center at Texas A&M University; adjustments by the Dallas Fed.

Provided by Federal Reserve of Dallas – Austin Economic Indicators – August 2020

HOUSING – PERMITS AND INVENTORY – AUSTIN

“The five-month moving average of total housing (single-family and multifamily) permits in Austin contracted 14.7 percent from May to June and was down 2.4 percent in the state (Chart 6). Austin’s existing-home inventories ticked down to 1.6 months, remaining well below the six months of supply considered to be a balanced market.”– Aug 2020 – Austin Economic Indicators – Dallas Fed

Housing Permits

Index, January 2005 = 100*



*Seasonally adjusted; five-month moving average.

SOURCE: Census Bureau.

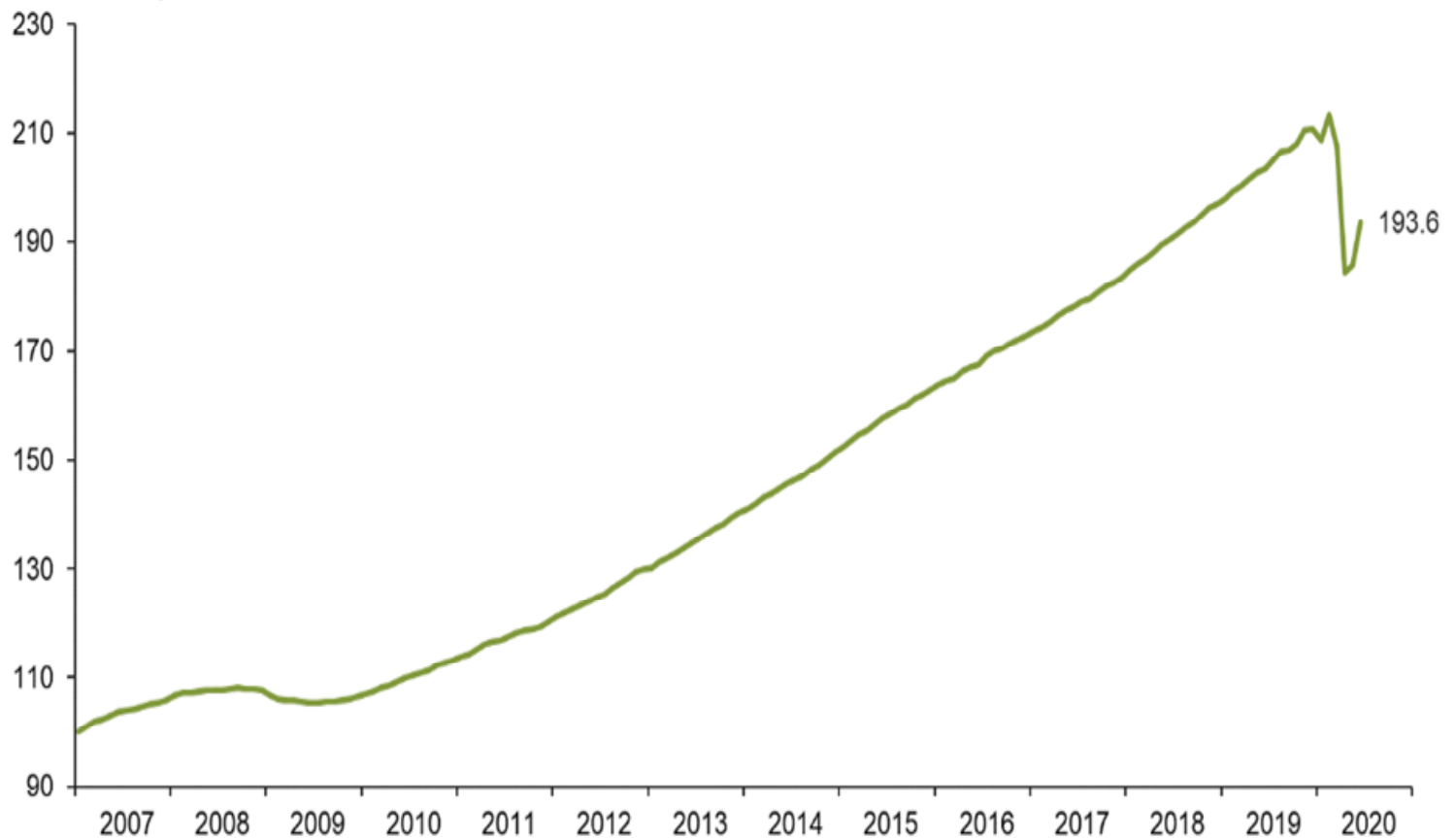
Provided by Federal Reserve of Dallas – Austin Economic Indicators – August 2020

BUSINESS CYCLE INDEX – AUSTIN MSA

“The Austin Business-Cycle Index – a broad measure of economic activity in the metro expanded an annualized 65.1 percent in June, suggesting an improvement in economic performance.” – Aug 2020 – Austin Economic Indicators – Dallas Fed

Austin Business-Cycle Index

Index, January 2007 = 100



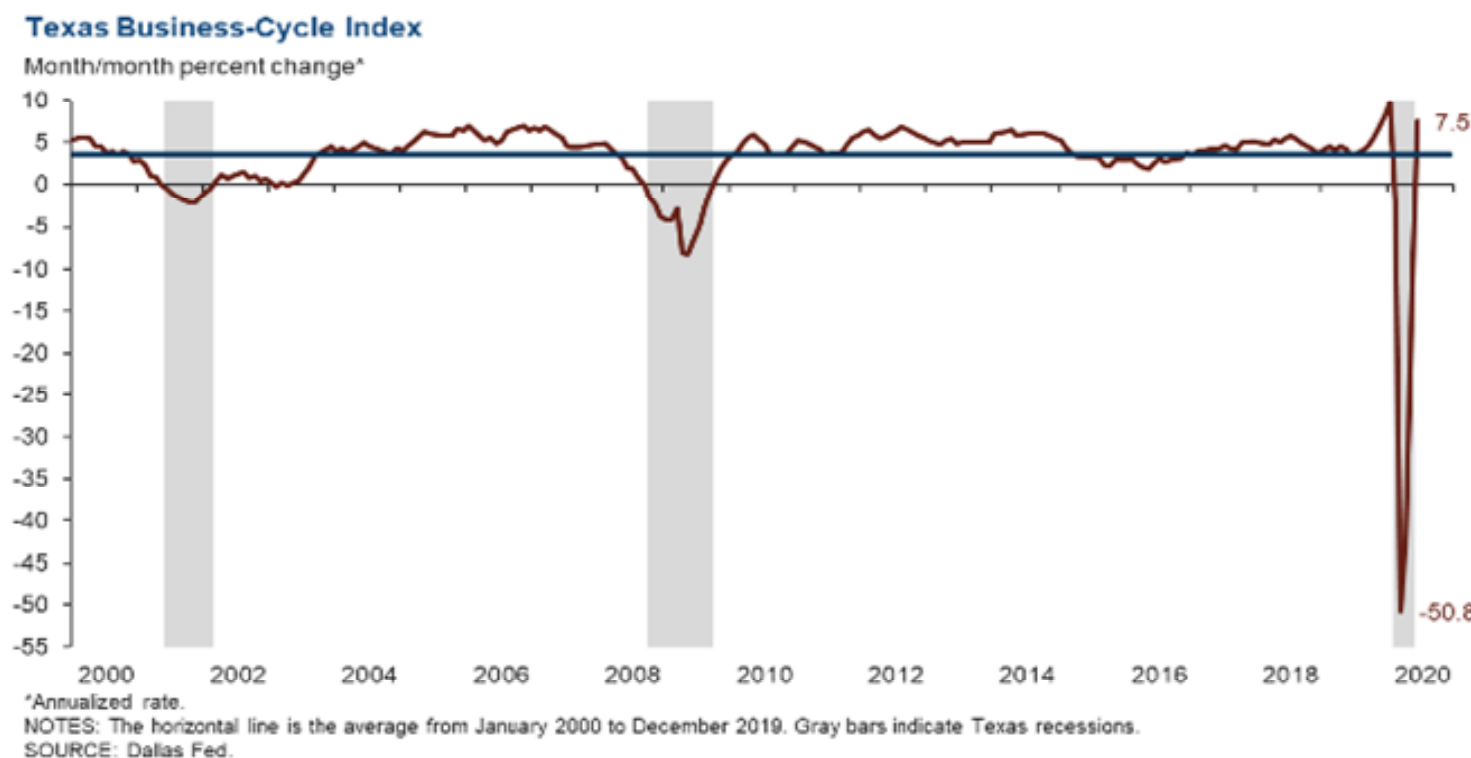
SOURCE: Dallas Fed.

Provided by Federal Reserve of Dallas – Austin Economic Indicators – Aug 2020

Business Cycle Indexes are meant to reflect broad movements in local economic conditions. The Dallas Fed states that “the [local area] indexes are constructed based on the aggregated movements in the local area unemployment rate, nonagricultural employment, inflation-adjusted wages, and inflation-adjusted retail sales. The weights of the components are statistically optimized for each metropolitan area in order to best capture the underlying cyclical movements in the local area economy.”

BUSINESS CYCLE INDEX – TEXAS

“The Texas Business-Cycle Index, a composite of the unemployment rate, state payroll employment and gross state product, measures underlying economic activity in the state. Heightened uncertainty due to the COVID-19 pandemic followed by an economic shutdown beginning in mid-March led to unprecedented declines in the index, sharper than those seen in the dot-com bubble or the Great Recession. The rate of contraction peaked in March when the index slipped 50.8 percent. The index continued to decline in April and May, though at a slower pace. In June, the index grew for the first time since January; however, it remains 7.4 percent below year-ago levels.” – Aug 2020 – Texas Economic Indicators – Dallas Fed



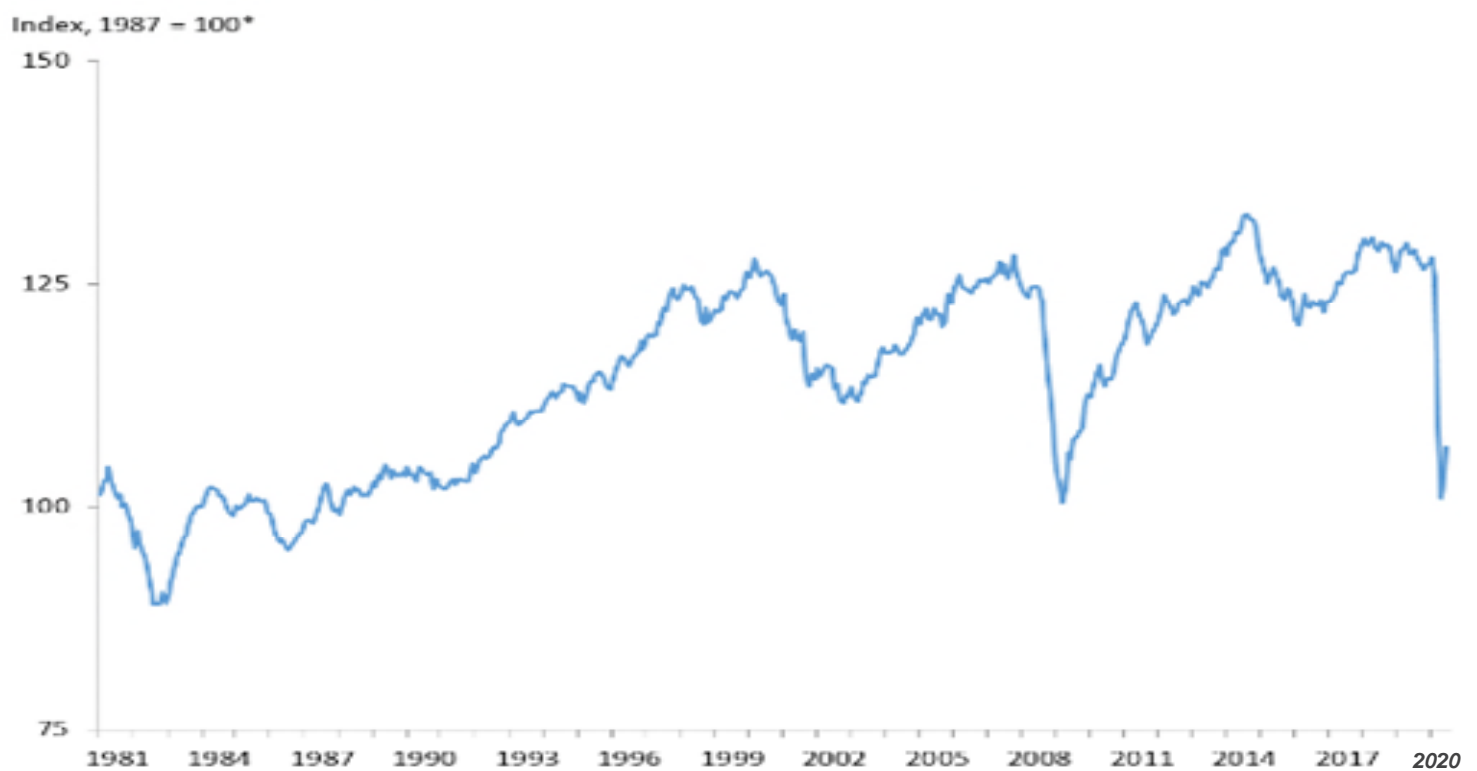
Provided by Federal Reserve of Dallas – Texas Economic Indicators – July 2020

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LEADING INDEX – TEXAS

“The Texas Leading Economic Index (a measure of future directional changes in the business cycle) improved for the second straight month after reaching a trough in April. Further declines in initial unemployment claims and recovery in the real oil price accounted for most of the increase.” – Aug 2020 – Real Estate Center – Texas A&M University

Texas Leading Index



*Monthly, seasonally adjusted.
Last data entry June 2020.
SOURCE: Federal Reserve Bank of Dallas.

Provided by Federal Reserve of Dallas – Regional Economic Data – July 2020

Dallas Fed has defined the **Texas Leading Index** as the “single summary statistic that sheds light on **the future of the State's economy**.” The Texas Leading Index is made up of eight leading indicators that have been shown to change direction – up or down – before the overall economy. The eight indicators used by the Dallas Fed are the Texas value of the dollar, U.S. leading index, real oil price, well permits, initial claims for unemployment insurance, Texas stock index, help-wanted index and average weekly hours worked in manufacturing.

STATE AND LOCAL CONSUMPTION AND GROSS INVESTMENT

“Over the four quarters ending in Q2, growth of real consumption at the state and local level was -1.47%, a rate of decline not seen since 2012. Consumption expenditures consist largely of employee salaries and make up over 80% of the sector’s total spending.

The 4-quarter change in state and local government gross investment spending was +2.8% in Q2, a sharp slowing from recent quarters. In order of importance, the categories of gross investment are new equipment (such as computers), intellectual property products (such as software), and public works and infrastructure projects.” – Aug 2020 – U.S. Economy in a Snapshot – NY Fed

Real State & Local Consumption & Gross Investment



Source: Bureau of Economic Analysis
via Haver Analytics

Note: Shading shows NBER recessions.

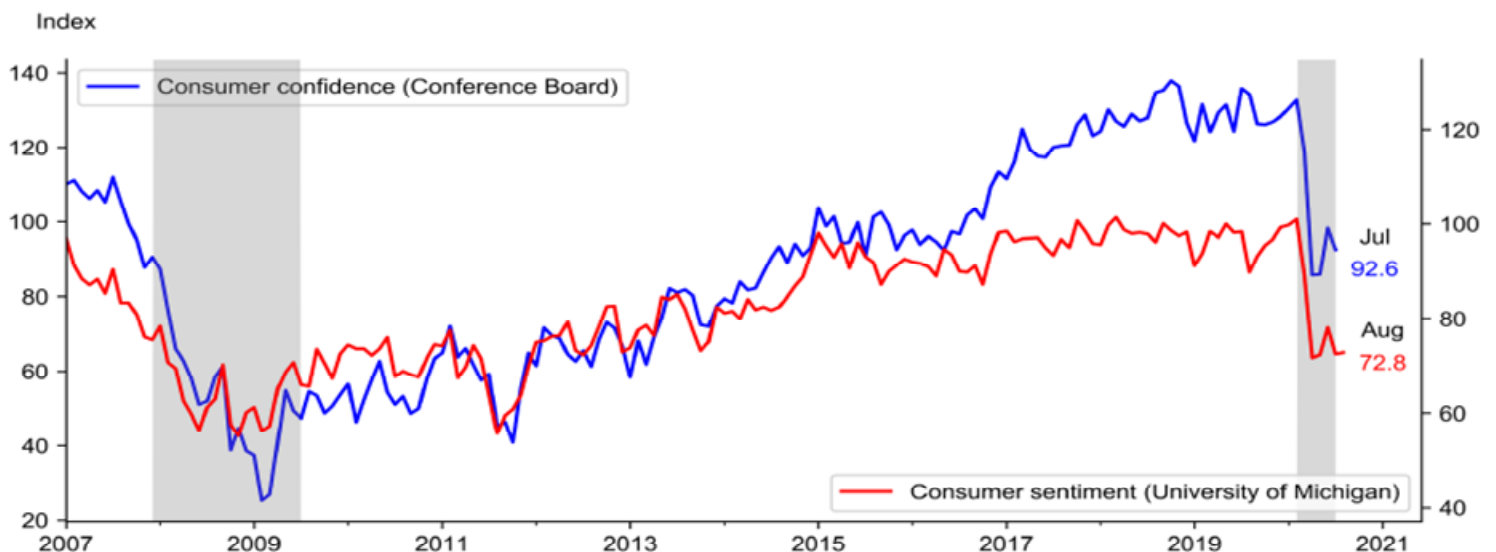
Provided by Federal Reserve of New York

CONSUMER CONFIDENCE AND SENTIMENT – U.S.

“Consumer Confidence declined in July following a large gain in June,” said Lynn Franco, Senior Director of Economic Indicators at The Conference Board. “The Present Situation Index improved, but the Expectations Index retreated. Large declines were experienced in Michigan, Florida, Texas and California, no doubt a result of the resurgence of COVID-19. Looking ahead, consumers have grown less optimistic about the short-term outlook for the economy and labor market and remain subdued about their financial prospects. Such **uncertainty about the short-term future does not bode well for the recovery, nor for consumer spending.**” – Jul 28, 2020 – The Confidence Board

Surveys of Consumers, Chief economist, Richard Curtin, commented “Consumer sentiment remained largely unchanged in early August from the July reading (+0.3 points) or the April low (+1.0). Two significant changes since April have been that **consumers have become more pessimistic about the five-year economic outlook (-18 points) and more optimistic about buying conditions (+21).** Lower interest rates by the Fed prompted more favorable buying, especially for homes, and the DC policy gridlock was responsible for the weaker outlook. **The overall confidence in economic policies fell to the lowest level since Trump first entered office.”**

Consumer Confidence



SOURCES: The Conference Board; University of Michigan.

Provided by Federal Reserve of Dallas – U.S. Economy Charts– Aug 2020

U.S. consumer **confidence** index (CCI) is defined as “**the degree of optimism on the [current] state of the economy** that consumers are expressing through their activities of savings and spending.” – Wikipedia

U.S. consumer **sentiment** is defined as “**the indicator of the future course of the national economy.**” – Investopedia

CREDIT AND DEBIT CARD SPENDING – TRAVIS COUNTY vs. TEXAS

“Consumer spending (measured by credit and debit card spending) in Travis County has improved significantly since early April. As of July 26, spending in the county was up 3.0 percent relative to January 2020, whereas spending in Texas was down 8.2 percent over the same period.” – Aug 2020 – Austin Economic Indicators – Dallas Fed

Credit and Debit Card Spending

Percent change relative to January 2020



NOTE: Data are daily through July 26, 2020.

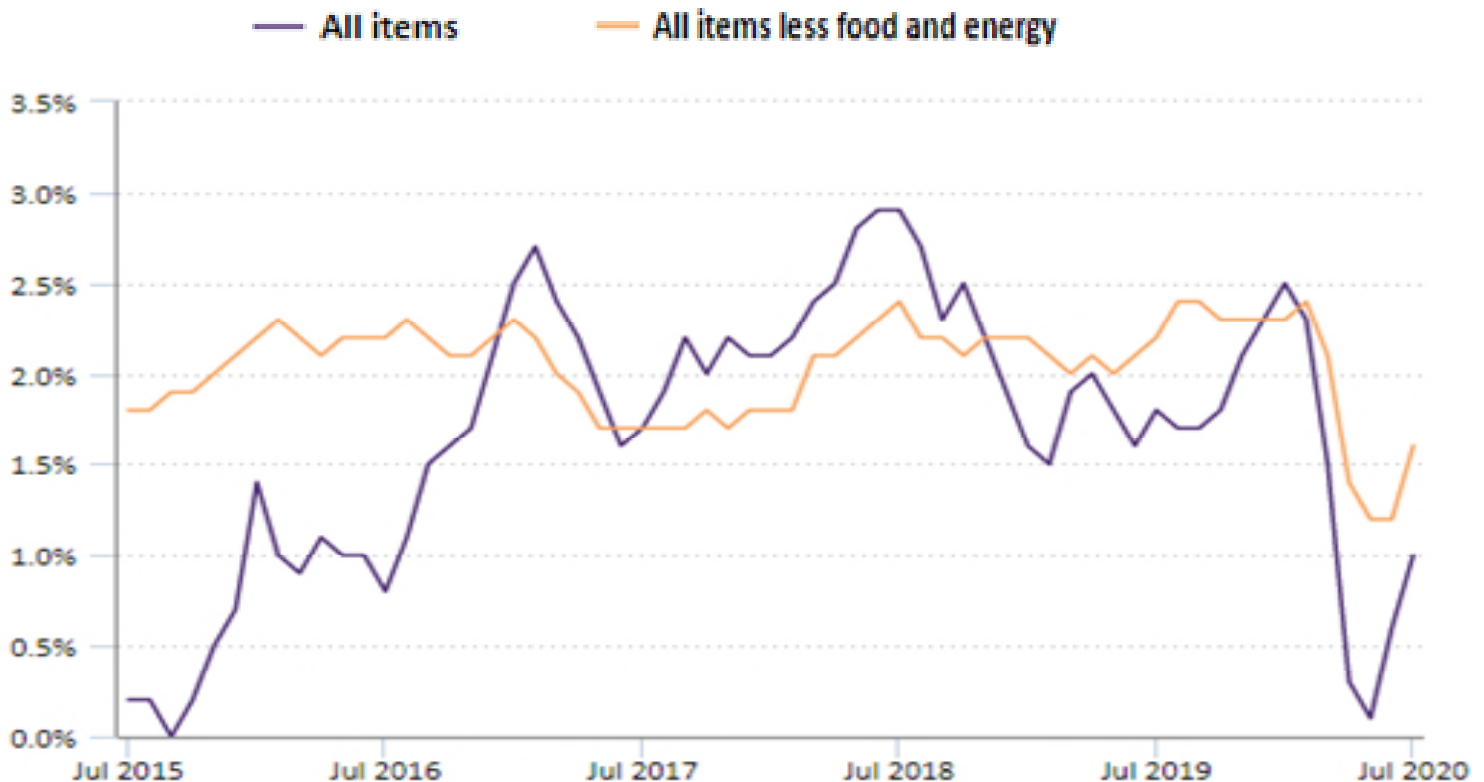
SOURCE: Tracktherecovery.org

Provided by Federal Reserve of Dallas – Austin Economic Indicators – Aug 2020

CONSUMER PRICE INDEX

“The all items index increased 1.0 percent for the 12 months ending July, a larger increase than the 0.6-percent rise for the period ending June. The index for all items less food and energy increased 1.6 percent over the last 12 months. The food index increased 4.1 percent over the last 12 months, with the index for food at home rising 4.6 percent. Despite increasing in July, the energy index fell 11.2 percent over the last 12 months.” – Bureau of Labor Statistics – Jul 2020 – Economic News Release

Consumer Price Index - 12 Month Percentage Change



Source: Bureau of Labor Statistics, not seasonally adjusted, 1982-84=100

According to the Bureau of Labor Statistics (BLS), “There are a variety of CPI numbers generated each month. In the graph above, two numbers are compared. The first is the **Official CPI Number** that is reported to the media. It is the broadest and most comprehensive CPI and is called the **All Items CPI for All Urban Consumers**. The second one is called the **All items less food and energy**.” The BLS mentions that “Some users of CPI data use this index because food and energy prices are relatively volatile, and these users want to focus on what they perceive to be the ‘core’ or ‘underlying’ rate of inflation.”

OIL AND NATURAL GAS PRICES

“At the onset of the coronavirus pandemic, oil prices consistently fell, while the number of people diagnosed with COVID-19 rose around the world. In late April, however, oil prices bottomed out and then began to recover, even as the COVID-19 case count continued to increase steadily. Oil prices recovered throughout May and have stabilized since. Natural gas prices have trended down over the long term before the COVID-19 pandemic. Since the outbreak, however, prices have hovered just under \$2 per million British thermal units. In the week ending July 17, prices ticked down.” – Jul 2020 – Texas Economic Indicators – Dallas Fed

Energy Prices



NOTE: Data are through the week ending July 17, 2020. Btu is British thermal units. Oil price is for West Texas Intermediate crude oil.

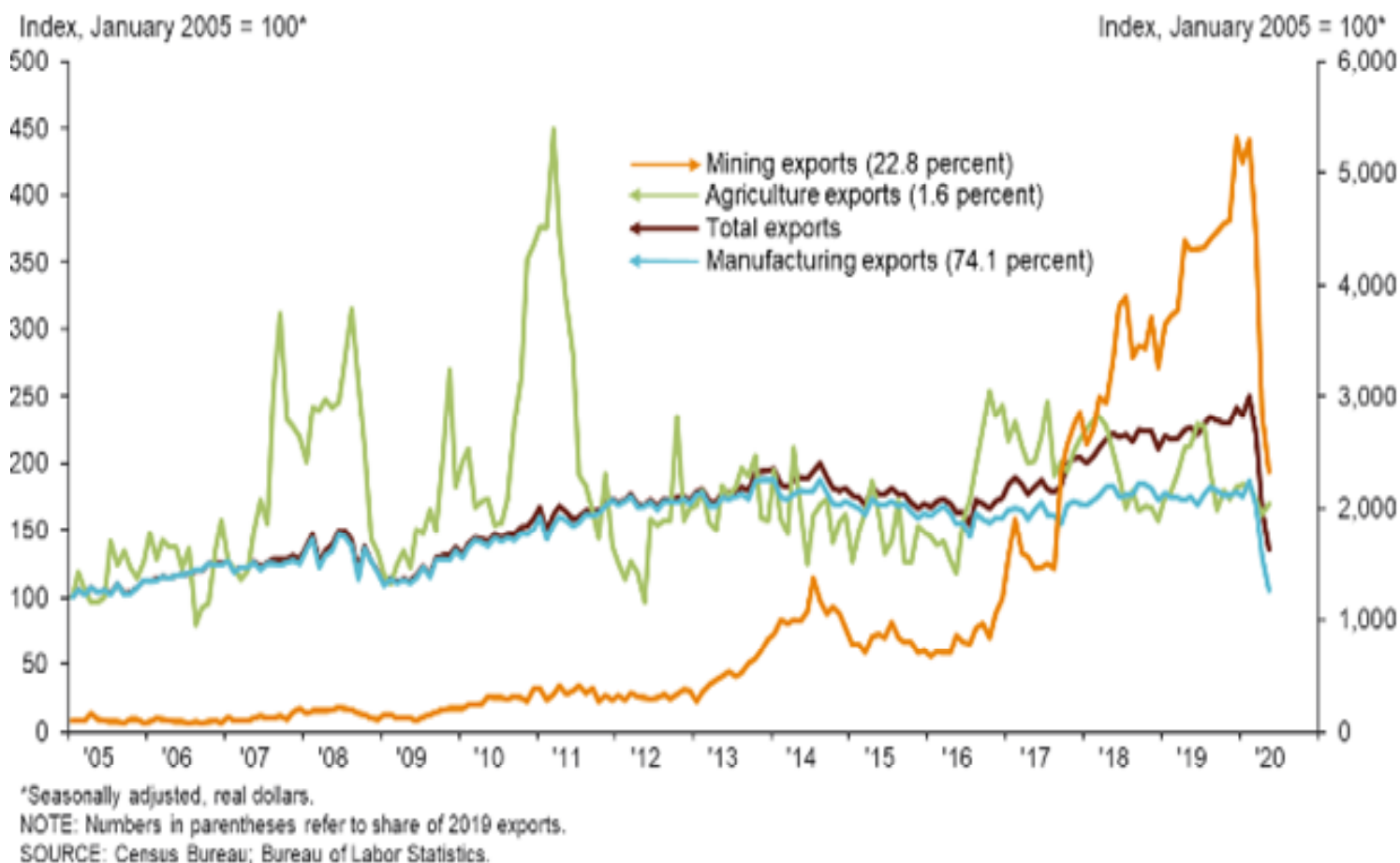
SOURCE: Energy Information Administration; Wall Street Journal.

Provided by Federal Reserve of Dallas – July 2020 - Texas Economic Indicators

TEXAS EXPORTS

“Texas exports in May fell for the third month in a row, sliding 18.2 percent. Hardest hit were manufacturing exports, followed by mining, which fell 19.6 percent and 17.8 percent, respectively. Agriculture exports grew modestly, climbing 4.7 percent. When compared with the impact of the Great Recession on exports in 2008–09, this pandemic has caused a much sharper decline in mining, manufacturing and total exports, while agriculture exports have been less impacted.” – Jul 2020 – Texas Economic Indicators – Dallas Fed

Texas Exports

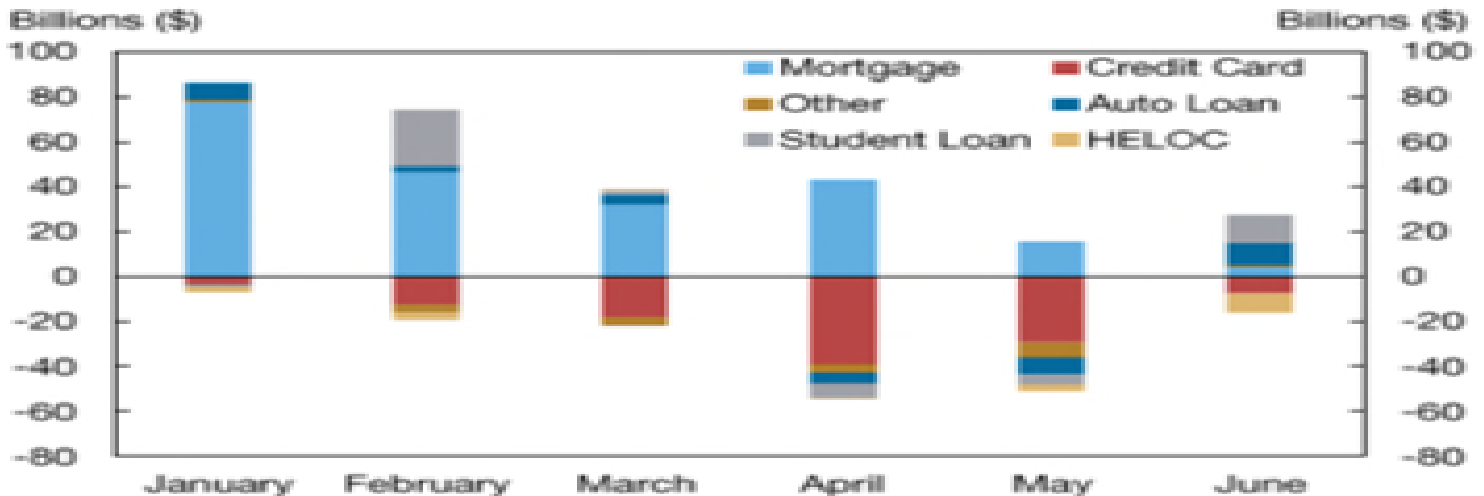


Provided by Federal Reserve of Dallas – July 2020 - Texas Economic Indicators

HOUSEHOLD DEBT

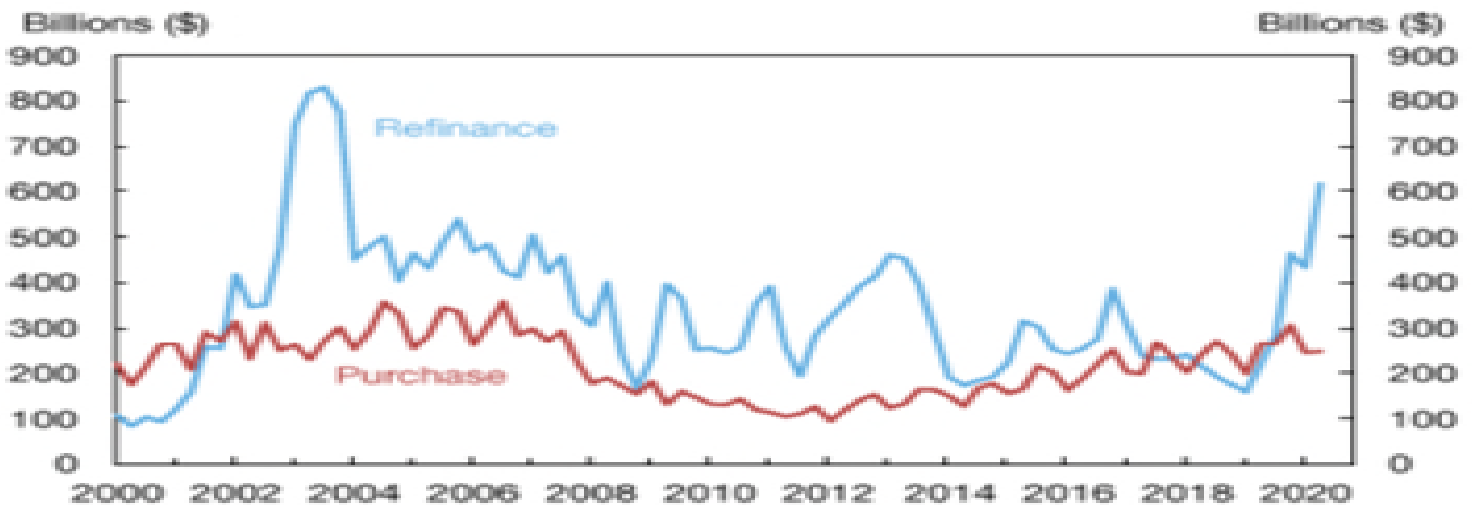
“The total outstanding household debt balance fell by \$34 billion in 2020 Q2. This decline, the first since 2014 Q2, was driven by a \$76 billion decline in card balances...” – Aug 2020 – U.S. Economy in a Snapshot – NY Fed

Contributions to Change in Debt Balances



Source: New York Fed Consumer Credit Panel/Equifax Provided by Federal Reserve of New York

Mortgage Originations



Source: New York Fed Consumer Credit Panel/Equifax Provided by Federal Reserve of New York

“Mortgage originations, in total, reached \$856 billion in the second quarter. Splitting into the two components – purchase originations and refinance originations – reveals very different trends. Mortgage refinances jumped notably, as many homeowners sought to refinance their existing mortgages and take advantage of low mortgage interest rates. Purchase originations were roughly stagnant” - Aug 2020 – U.S. Economy in a Snapshot – NY Fed

GDP GROWTH – UNITED STATES

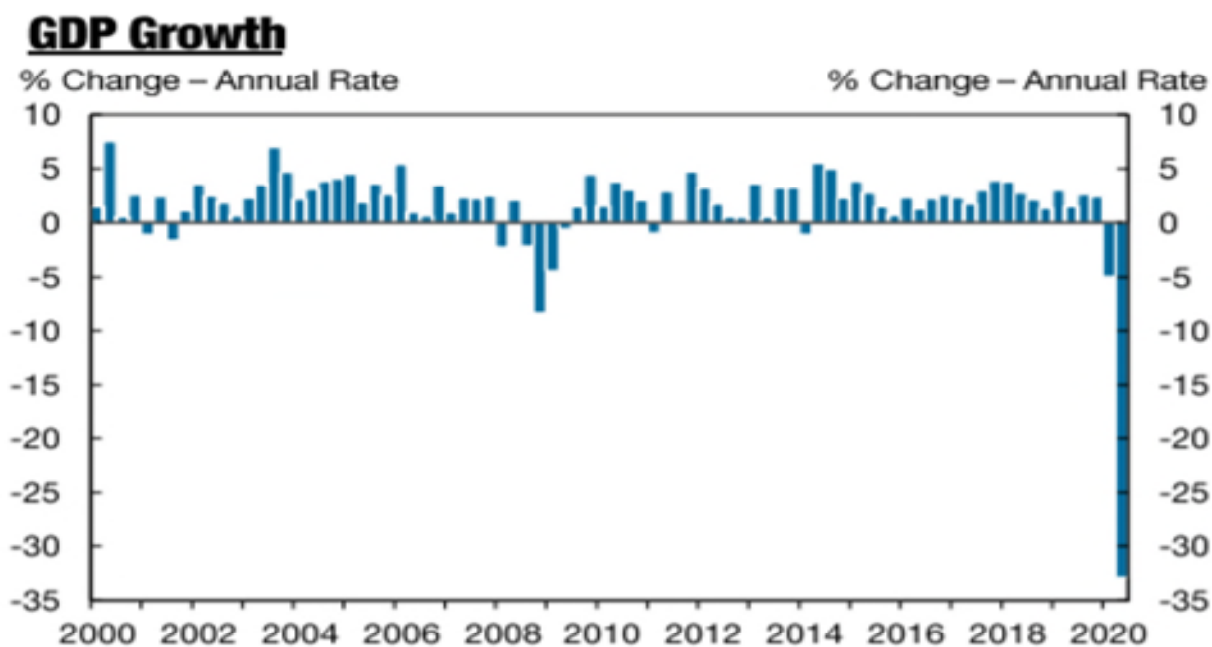
“Real GDP plunges in 2020 Q2. In the BEA’s first estimate, real GDP plummeted at a -32.9% annual rate (-9.5% at a quarterly rate) in 2020 Q2, the most severe fall in the post-war era. The 4-quarter change was 9.5%.

Real personal consumption expenditures fell at a 34.5% annual rate in Q2, its largest decline. The decline was most severe affected by COVID measures.

There were also large declines in business investment, residential investment, exports and imports.

Federal government expenditures rose, reflecting spending associated with the PPP program. State and local government expenditures fell.

Personal income rose in the quarter because of COVID related transfers. The personal saving rate rose to 25.7%.” – Aug 2020 – U.S. Economy in a Snapshot – NY Fed



Source: Bureau of Economic Analysis via Haver Analytics

Provided by Federal Reserve of New York

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

INTRODUCTION

“When the **Small Business Reorganization Act (SBRA)** was signed into law in August 2019 and slated to go effective in February 2020, no one could have foreseen that, by March 2020, the U.S. economy would grind to a halt as a result of a global pandemic. The financial consequences of COVID-19 have hit small businesses especially hard. The SBRA – commonly known as Subchapter V, referring to **new Subchapter V of Chapter 11 of the Bankruptcy Code** – **may provide a much-needed lifeline to small businesses struggling to survive this crisis**. With Subchapter V elections likely to surge during and after the pandemic, lenders and other creditors should know how the SBRA alters the normal Chapter 11 landscape to which they may be accustomed.

Arguably, the SBRA was long overdue. Many financially distressed small businesses have consulted a bankruptcy lawyer only to learn that, ironically, they are too poor to reorganize under Chapter 11. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) promised to streamline Chapter 11 for small businesses, for example, by allowing a one-step plan solicitation and confirmation process. However, BAPCPA imposed increased reporting requirements and other procedural burdens that many felt outweighed the benefits for small businesses.” – Apr 2020 – White and Williams LLP

“Smaller companies that did file often failed to survive, even after Congress’s earlier reform in 2005. Of the more than 18,000 small businesses that filed for chapter 11 from 2008 to 2015, only about 27% received a judge’s approval for their reorganization plan, Maine bankruptcy lawyer Bob Keach told Congress last year.” – May 2020 - Marketwatch

“**The general purpose of Subchapter V was to streamline the Chapter 11 bankruptcy process for small businesses and individuals engaged in business to administer their bankruptcy estate in an efficient and less costly manner.**” – Jun 2020 – New York Law Journal

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

BEFORE SBRA – TWO OPTIONS – CHAPTER 7 OR CHAPTER 11

“Before SBRA, struggling businesses considering bankruptcy had two options: chapter 7 or chapter 11. Upon the filing of a chapter 7 case, a bankruptcy estate is created that is comprised of the debtor's nonexempt property. A trustee is appointed to liquidate the assets of the bankruptcy estate and distribute the proceeds to the debtor's creditors. **Chapter 7 is not an option for businesses hoping to survive bankruptcy and retain control of its operations.**

In contrast, a chapter 11 debtor retains control over its operations and restructures its debts through a court-approved plan. **Although the chapter 11 debtor retains control, the debtor is subject to increased oversight from the bankruptcy court and the U.S. trustee.** The chapter 11 debtor's plan to repay its debts must meet stringent requirements and be confirmed (i.e., approved) by the bankruptcy court before the debtor can exit bankruptcy. While in bankruptcy, the debtor is required to obtain the court's approval of all non-ordinary course-of-business transactions and must comply with the U.S. trustee's monthly reporting requirements. **As a result, a small business may not be able to afford the costs of a chapter 11.**

The SBRA endeavors to strike a balance between chapter 7 and chapter 11. **Under the SBRA, certain debtors can retain control over their business operations while reorganizing. However, they will no longer be subject to the more costly requirements in chapter 11.** Unlike chapter 11, a trustee will be appointed to each small-business debtor case. The SBRA's sponsors explain that the trustee will ‘perform duties similar to those performed by a . . . Chapter 13 trustee and help ensure the reorganization stays on track.’” – Feb 2020 – American Bar Association

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

WHO QUALIFIES FOR SBRA?

“Prior to the SBRA, ‘small business debtor’ meant a debtor who:

- Is engaged in commercial business activities
- With aggregate non-contingent, liquidated debt of not more than \$2,725,625 excluding debts owed to affiliates or insiders

Excluded from the definition were owners and operators of real property and any member of a group of affiliated debtors with aggregate debt greater than \$2,725,625.

The SBRA modified the definition of ‘small business debtor,’ and to qualify under the SBRA:

- 50% or more of the debtors’ prepetition debts must arise from the commercial or business activities of the debtor
- Single asset real estate debtors, public companies and their affiliates are excluded
- For small business debtors that elect Subchapter V, the CARES Act raised the debt limit from \$2,725,625 to \$7,500,000 until March 27, 2021 ^[1]
- In addition to corporations (including LLCs) and partnerships, sole proprietorships may also file under Subchapter V” – June 2020 – Cooley Alert

^[1] “Some cynics have speculated that, for borrowers on the cusp, lenders may extend additional credit to disqualify the borrower from a Subchapter V election. On the flipside, since the limit applies to ‘non-contingent’ debt, desperate or unscrupulous debtors could potentially circumvent the limit by characterizing legitimate debts as contingent or disputed.”

- White and Williams LLP

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

HOW DOES THE LAW HELP SMALL BUSINESSES IN BANKRUPTCY?

1. Helps business owners maintain control

Subchapter V procedures for reorganizing “change dozens of different elements of a traditional reorganization; **the biggest advantage for debtors may be that they have a far better chance of holding on to their company.** In a traditional Chapter 11 reorganization, the bankrupt company's equity owners usually get no stake in the reorganized enterprise unless all of its debts are repaid in full.

Now business owners can keep their equity, so long as they distribute their disposable income to creditors over the next three to five years. ‘The goal of the Subchapter V is to let the small business owner remain in possession of the assets,’ says Deborah Williamson, who heads the bankruptcy practice at the law firm Dykema. ‘That's a different goal than the bankruptcy goal.’” – Apr 2020 – Bloomberg Businessweek

2. Allows modification of residential mortgages

“Subchapter V also cushions small business owners from certain adverse personal consequences that might otherwise disincentivize a Chapter 11 filing.”– Apr 2020 – White and Williams LLP

“Notably, the act **[removes] the categorical prohibition against individual small business debtor’s modifying their residential mortgages.** The act now allows a small business debtor to modify a mortgage secured by a residence if the underlying loan was not used to acquire the residence and was primarily used in connection with the small business of the debtor. Otherwise, secured lenders have the same protections as in other Chapter 11 cases.” – Aug 2019 – Financial Services Perspective

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

HOW DOES THE LAW HELP SMALL BUSINESSES IN BANKRUPTCY? (cont.)

3. Balances the power of creditors

“The SBRA makes it possible for equity interests to be maintained without agreement from creditors who may receive less than a full recovery on account of their claims.” – Jun 2020 – Cooley

“Legal scholars said small-business owners often couldn’t comply with the previous law’s requirement that they either repay all debt to retain ownership or convince creditors to accept less. **That rule gave unhappy holdout creditors that power to object, leading the business to shut down or look for buyers.**” – May 2020 – Marketwatch

“**‘Almost by definition, when you get to the point that you’re filing to stop a foreclosure, you’re at odds with the lender,’** says San Antonio bankruptcy lawyer Ray Battaglia. ‘They don’t want to deal with it. They don’t trust you. They don’t believe your credibility.’” – Apr 2020 –Bloomberg Businessweek

“Under the new law, businesses are still required to fully repay taxes, loans and other forms of secured debt. But for unsecured debt—money owed to vendors, customers and other business partners—bankrupt small-business owners can retain ownership if they promise to use future profits to pay a portion of that debt through monthly payments.” – May 2020 - Marketwatch

“[U]nder Subchapter V, with the repayment plan in place that includes full repayment of debt secured with collateral, a court will confirm the plan over this opposition. **Under the new system, ‘I can have every creditor voting against me and still theoretically confirm a plan,’** Battaglia says. Only debtors—not creditors or other interested parties—may propose a plan under Subchapter V.” – Apr 2020 –Bloomberg Businessweek

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

HOW DOES THE LAW HELP SMALL BUSINESSES IN BANKRUPTCY? (cont.)

4. Potentially reduces the cost of a bankruptcy

“As part of the rules change, companies must file debt repayment plans more quickly, which is aimed at preventing bankruptcy attorneys from dragging out the process to boost their fees.” – May 2020 – Marketwatch

“Small businesses no longer need to pay Justice Department fees or file a formal disclosure statement, a legal document that lawyers charge thousands of dollars to write up.” – May 2020 – Marketwatch

“It **eliminates**—for all small-business cases, not just those pursued under Subchapter V—the **automatic creation of creditors' committees (with attorneys' and other professional fees paid by the debtor)** unless the court similarly orders them. And the debtor's reorganization plan doesn't have to be nearly as detailed as in a typical Chapter 11 proceeding.” – Apr 2020 –Bloomberg Businessweek

“In a chapter 11 case, the debtor's exclusive right to file a plan is limited. Once this exclusivity period expires, creditors are free to file their own competing plans. The SBRA permits only the debtor to file a plan of reorganization. The SBRA's elimination of a disclosure statement and potential competing plans will prevent contested hearings that prolong the reorganization process and increase costs for debtors.” – Feb 2020 – American Bar Association

“One Georgia manufacturer said the new rules cut its estimated bankruptcy costs from \$50,000 down to \$15,000. Several lawyers said they have started taking cases for small businesses that previously couldn't afford their services, including Richard Banks, who represents Mr. Brown's company.” – May 2020 – Marketwatch

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

HOW DOES THE LAW HELP SMALL BUSINESSES IN BANKRUPTCY? (cont.)

5. Provides for a trustee

“It also gives small-business owners access to a court-appointed financial expert to help fix their problems.” – May 2020 – Marketwatch

“Normally, a Chapter 11 trustee is appointed only for cause, such as fraud or gross mismanagement, and seizes control of the debtor’s operations. **Under Subchapter V, a trustee is automatically appointed, but the debtor retains control of its assets and operations.** Creditors’ committees – a staple in traditional Chapter 11 cases – are formed only for cause in Subchapter V cases. Although Subchapter V trustees have authority to investigate the debtor’s financial affairs, **their primary function is to facilitate a consensual plan among the debtor and its creditors, almost like a mediator would facilitate a settlement in litigation.**

The involvement of an impartial third-party may increase the likelihood of a fair and equitable resolution among the debtor and its creditors, and may be particularly useful for a small business whose creditors are unwilling to make reasonable concessions in light of the impending financial crisis. Under the supervision of the Department of Justice, approximately 250 Subchapter V trustees – mostly attorneys and accountants – were selected out of over 3,000 applicants. Most Subchapter V trustees had recently received their first case assignments when the COVID-19 pandemic hit.” – Apr 2020 – White and Williams LLP

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

DEBTORS MAY BE INELIGIBLE TO RECEIVE PPP LOANS

“The debt ceiling for a small business to file under Subchapter V was recently increased temporarily to \$7.5 million under the Coronavirus Aid, Relief and Economic Security act of 2020 (the CARES Act). This debt ceiling increase expands access to bankruptcy relief to thousands of small businesses.

However, there is a remarkable irony between the laudable purpose of this legislation to help small businesses navigate efficiently through bankruptcy and its execution in the COVID-19 environment. One fly in the ointment is whether small business debtors can use PPP loans in bankruptcy.

By way of background, the CARES Act provided \$349 billion for financing ‘small businesses’ under the Paycheck Protection Program (PPP). Under the PPP, eligible small businesses are entitled to receive loans up to \$10 million guaranteed by the Small Business Administration (SBA).

Neither the CARES Act nor the Small Business Act, however, expressly prohibits companies who have filed for bankruptcy from receiving PPP loans but this is undercut by the fact that the SBA requires that lenders use an SBA loan application form that expressly disqualifies any small business in bankruptcy. To reinforce this position the SBA promulgated an interim final rule that makes debtors ineligible to receive PPP loans.

The reason for the rule was that PPP loans to entities in bankruptcy would present an unacceptably high risk of an ‘unauthorized use’ of funds or non-repayment of unforgiven loans. But does this make sense? Under the CARES Act, PPP loans are really not loans, but instead are treated as grants if 75% of the loan proceeds are used for payroll and the remaining 25% for rent, utilities and other operating expenses. If the borrower complies with these guidelines, the loan essentially will be forgiven.” – Jun 2020 – Law.com – New York Law Journal

IN-DEPTH – SMALL BUSINESS REORGANIZATION ACT

CONCLUSION

“Legal commentators have long lamented that chapter 11's high costs and complexities make it too difficult for small businesses to successfully reorganize. In response to these concerns, Congress recently passed amendments to the Bankruptcy Code known as the Small Business Reorganization Act (SBRA).” – Feb 2020 – American Bar Association

“Over time the benefits of Subchapter V should provide small business with a realistic chance to restructure debt and reorganize their business, thereby preserving enterprise value, maintaining business relationships and savings jobs.” – June 2020 – Law.com – New York Law Journal

IN-DEPTH TOPICS LOCATED ON THE COUNTY AUDITOR'S WEBPAGE

• 5G Network	4 th Qtr 2018
• Alibaba	3 rd Qtr 2017
• Bitcoin	4 th Qtr 2016
• Cashless Society	4 th Qtr 2017
• Chatbots	1 st Qtr 2019
• Facial Recognition	1 st Qtr 2018
• Labor Participation Rate	4 th Qtr 2015
• Libra, Calibra, Facebook	2 nd Qtr 2019
• Money Market Fund Reform – New Rules	3 rd Qtr 2016
• Natural Gas – U.S. 3 RD Largest Exporter of LNG	4 th Qtr 2019
• Negative Interest Rate Policy (NIRP)	2 nd Qtr 2016
• New Silk Road	2 nd Qtr 2017
• Pandemic – Possible Impact	1 st Qtr 2020
• Quantitative Easing	1 st Qtr 2016
• Repurchase Agreements – Repo Market in Crisis	3 rd Qtr 2019
• Small Business Reorganization Act	2 nd Qtr 2020
• Texas Imports and Exports	2 nd Qtr 2018
• Universal Postal Union	3 rd Qtr 2018

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